(14) (19)

Nos. 03-892 and 03-907

OCT 22 2004

In The
Supreme Court of the United States

COMMISSIONER OF INTERNAL REVENUE,

Petitioner,

v.

JOHN W. BANKS, II

COMMISSIONER OF INTERNAL REVENUE,

Petitioner,

v.

SIGITAS J. BANAITIS

On Writs Of Certiorari To The United States Courts Of Appeals For The Sixth And Ninth Circuits

JOINT SUPPLEMENTAL BRIEF FOR RESPONDENTS

PHILIP N. JONES
Counsel of Record for Respondent Banaitis in 03-907
DUFFY KEKEL LLP
1200 Standard Plaza
1100 S.W. Sixth Avenue
Portland, OR 97204
(503) 226-1371

RUSSELL R. YOUNG
Counsel of Record for Respondent Banks in 03-892
MAYER, BROWN, ROWE & MAW, LLP
190 South LaSalle Street
Chicago, IL 60603
(312) 701-7745

COCKLE LAW BRIEF PRINTING CO. (800) 225-6964
OR CALL COLLECT (402) 342-2831

JOINT SUPPLEMENTAL BRIEF FOR RESPONDENTS

Pursuant to Rule 25.5 of this Court, Respondents in the above-entitled cases, which have been consolidated for oral argument on November 1, 2004, submit the following joint supplemental brief. The purpose of this supplemental brief is to call to the Court's attention newly enacted legislation, which the president signed into law October 22, 2004. While the new legislation is not retroactive, it nevertheless will limit sharply the impact of any decision rendered by the Court in future cases involving substantially the same facts. There is thus a possibility that the Court may conclude, upon examination of the new legislation, that both cases should be dismissed on the ground that the writs of certiorari were improvidently granted.

On October 22, 2004, the president signed the *American Jobs Creation Act of 2004*. Section 703 of the Act, entitled Civil Rights Tax Relief, amends section 62(a) of the Internal Revenue Code by expressly permitting a taxpayer to subtract from his or her gross income, in arriving at adjusted gross income, the "attorneys fees and court costs paid by, or on behalf of, the taxpayer in connection with any action involving a claim of unlawful discrimination" as defined by the Act. Section 62(e) of the Internal Revenue Code, as amended by the Act, defines the term "unlawful discrimination" as an act that is unlawful under various enumerated federal, state, and local statutory provisions, as well as common law claims. Section 703 is reproduced in an Appendix to this Supplemental Brief.

Significantly, Internal Revenue Code section 62(a), as amended by the Act, includes as "unlawful discrimination"

acts which gave rise to the tax disputes in both Respondents Banks's and Banaitis's respective cases. Respondent Banks's underlying discrimination claims, which gave rise to his current tax dispute with Petitioner, were based on violations of: (1) Title VII of the Civil Rights Act of 1964, as amended, 42 U.S.C. section 2000e *et seq.*; and (2) 42 U.S.C. sections 1981 and 1983. No. 03-892, Pet. App. 1a-5a. Internal Revenue Code sections 62(e)(13) and (14), as amended by the Act, expressly include as "unlawful discrimination" acts which violate 42 U.S.C. section 2000e-2, 2000e-3, 2000e-16, and 42 U.S.C. sections 1981 and 1983. Moreover, Respondent Banaitis's underlying claims, which gave rise to his current tax dispute with Petitioner, were based on state common law claims for wrongful discharge and tortious interference with contract by his former employer. No. 03-907, Pet. App. 4a. Internal Revenue Code section 62(e)(18)(ii) expressly includes as "unlawful discrimination" "[a]ny provision of * * * State, or local law, or common law claims permitted under * * * State, or local law – regulating any aspect of the employment relationship, including claims for wages, compensation, or benefits, or prohibiting the discharge of any employee."

The new legislation applies to attorneys fees paid after the date of enactment with respect to any settlement or judgment occurring after its enactment. The new legislation thus does not apply to Respondent Banks's or Banaitis's respective tax disputes with Petitioner. However, any decision of this Court will have little or no impact on future tax disputes involving substantially the same facts. Moreover, prudential considerations, including deference to the coordinate branches, may warrant a

determination that a decision as to the merits should not be reached in either of these cases. A decision on the merits in favor of Petitioner in either or both cases would lead to disparate tax consequences for federal and state discrimination claimants, depending on the date when judgment was rendered or settlement was reached with respect to their claims.

A final consideration which may warrant dismissal in each case on the ground that the writ of certiorari was improvidently granted is that Sen. Charles Grassley, the Chairman of the Senate Finance Committee, stated on the Floor of the Senate, shortly following passage of the Act by Congress, that the portion of the Act relevant to each of these cases was designed to *clarify* and not change existing law, and that judgments rendered or settlements reached prior to the effective date of the Act should be treated identically as judgments and settlements subject to the Act:

> Mr. BAUCUS. As I understand it, the case law with respect to the tax treatment of attorney's fees paid by those that receive settlements or judgments in connection with a claim of unfaithful discrimination, a False Claims Act, "Qui Tam," proceeding or similar actions is unclear and that its application was questionable as interpreted by the IRS. Further it was never the intent of Congress that the attorneys' fees portions of such recoveries should be included in taxable income whether for regular income or alternative minimum tax purposes.

> Is it the understanding of the chairman that it was the conferees' intention for Section 703 to clarify the proper interpretation of the prior law, and any settlements prior to the date of enactment should be treated in a manner consistent with such intent?
>
> Mr. GRASSLEY. The Senator is correct. The conferees are acting to make it clear that attorneys' fees and costs in these cases are not taxable income, especially where the plaintiff, or in the case of a Qui Tam proceeding, the relator, never actually receives the portion of the award paid to the attorneys. Despite differing opinions by certain jurisdictions and the IRS, it is my opinion that this is the correct interpretation of the law prior to enactment of Section 703 as it will be going forward. In adopting this provision, Congress is codifying the fair and equitable policy that the tax treatment of settlements or awards made after or prior to the effective date of this provision should be the same. The courts and IRS should not treat attorneys' fees and other costs as taxable income.
>
> * * *
>
> [I]t is my strong belief that the courts and the IRS should apply the guidelines of Section 703 not only after the date of enactment but also to settlements put in place prior to that time.

150 CONG. REC. S11036 (daily ed. October 10, 2004). A dismissal would thus be consistent with that legislative history, because both Banks and Banaitis prevailed below.

For the foregoing reasons, the late developments described above may warrant dismissal of both of the consolidated cases on the ground that the writs of certiorari were improvidently granted.

Respectfully submitted,

RUSSELL R. YOUNG
Counsel of Record for
Respondent Banks in 03-892
MAYER, BROWN, ROWE &
MAW, LLP
190 South LaSalle Street
Chicago, IL 60603
(312) 701-7745

PHILIP N. JONES
Counsel of Record for
Respondent Banaitis in 03-907
DUFFY KEKEL LLP
1200 Standard Plaza
1100 S.W. Sixth Avenue
Portland, OR 97204
(503) 226-1371

OCTOBER 2004

APPENDIX

Citations: H.R. 4520;
American Jobs Creation Act of 2004

Date: Oct. 7, 2004

SECTION 1. SHORT TITLE; ETC.

(a) SHORT TITLE. – This Act may be cited as the "American Jobs Creation Act of 2004".

(b) AMENDMENT OF 1986 CODE. – Except as otherwise expressly provided, whenever in this Act an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1986.

* * *

SEC. 703. CIVIL RIGHTS TAX RELIEF.

(a) DEDUCTION ALLOWED WHETHER OR NOT TAXPAYER ITEMIZES OTHER DEDUCTIONS. – Subsection (a) of section 62 (defining adjusted gross income) is amended by inserting after paragraph (18) the following new item:

"(19) COSTS INVOLVING DISCRIMINATION SUITS, ETC. – Any deduction allowable under this chapter for attorney fees and court costs paid by, or on behalf of, the taxpayer in connection with any action involving a claim of unlawful discrimination (as defined in subsection (e)) or a claim of a violation of subchapter III of chapter 37 of title 31, United States Code or a claim made under section 1862(b)(3)(A) of the Social Security Act (42 U.S.C. 1395y(b)(3)(A)). The preceding sentence shall not apply to any deduction in excess of the amount includible in the taxpayer's gross income for the taxable year on account of

a judgment or settlement (whether by suit or agreement and whether as lump sum or periodic payments) resulting from such claim."

(b) UNLAWFUL DISCRIMINATION DEFINED. – Section 62 is amended by adding at the end the following new subsection:

"(e) UNLAWFUL DISCRIMINATION DEFINED. – For purposes of subsection (a)(19), the term 'unlawful discrimination' means an act that is unlawful under any of the following:

"(1) Section 302 of the Civil Rights Act of 1991 (2 U.S.C. 1202).

"(2) Section 201, 202, 203, 204, 205, 206, or 207 of the Congressional Accountability Act of 1995 (2 U.S.C. 1311, 1312, 1313, 1314, 1315, 1316, or 1317).

"(3) The National Labor Relations Act (29 U.S.C. 151 et seq.).

"(4) The Fair Labor Standards Act of 1938 (29 U.S.C. 201 et seq.).

"(5) Section 4 or 15 of the Age Discrimination in Employment Act of 1967 (29 U.S.C. 623 or 633a).

"(6) Section 501 or 504 of the Rehabilitation Act of 1973 (29 U.S.C. 791 or 794).

"(7) Section 510 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1140).

"(8) Title IX of the Education Amendments of 1972 (20 U.S.C. 1681 et seq.).

"(9) The Employee Polygraph Protection Act of 1988 (29 U.S.C. 2001 et seq.).

"(10) The Worker Adjustment and Retraining Notification Act (29 U.S.C. 2102 et seq.).

"(11) Section 105 of the Family and Medical Leave Act of 1993 (29 U.S.C. 2615).

"(12) Chapter 43 of title 38, United States Code (relating to employment and reemployment rights of members of the uniformed services).

"(13) Section 1977, 1979, or 1980 of the Revised Statutes (42 U.S.C. 1981, 1983, or 1985).

"(14) Section 703, 704, or 717 of the Civil Rights Act of 1964 (42 U.S.C. 2000e-2, 2000e-3, or 2000e-16).

"(15) Section 804, 805, 806, 808, or 818 of the Fair Housing Act (42 U.S.C. 3604, 3605, 3606, 3608, or 3617).

"(16) Section 102, 202, 302, or 503 of the Americans with Disabilities Act of 1990 (42 U.S.C. 12112, 12132, 12182, or 12203).

"(17) Any provision of Federal law (popularly known as whistleblower protection provisions) prohibiting the discharge of an employee, the discrimination against an employee, or any other form of retaliation or reprisal against an employee for asserting rights or taking other actions permitted under Federal law.

"(18) Any provision of Federal, State, or local law, or common law claims permitted under Federal, State, or local law –

"(i) providing for the enforcement of civil rights, or

"(ii) regulating any aspect of the employment relationship, including claims for wages, compensation, or benefits, or prohibiting the discharge of an employee, the discrimination against an employee, or any other form of retaliation or reprisal against an employee for asserting rights or taking other actions permitted by law.".

(c) EFFECTIVE DATE. – The amendments made by this section shall apply to fees and costs paid after the date of the enactment of this Act with respect to any judgment or settlement occurring after such date.